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REPORT OF THE SECRETARY-GENERAL ON THE ACTIVITIES OF THE OFFICE OF INTERNAL OVERSIGHT SERVICES

Note by the Secretary-General

Pursuant to General Assembly resolution 48/218 B of 29 July 1994, the Secretary-General has the honour to transmit, for the attention of the General Assembly, the attached report, conveyed to him by the Under-Secretary-General for Internal Oversight Services, on the audit of procurement handled by the Contracts and Procurement Service of the Department for Development Support and Management Services. The Secretary-General concurs with the recommendations in the report.

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ANNEX

Audit of procurement handled by the Contracts and Procurement Service of the Department for Development Support and Management Services

Report of the Office of Internal Oversight Services

I. INTRODUCTION

1. An audit of the procurement handled by the Contracts and Procurement Service of the Department for Development Support and Management Services, (DDSMS) was carried out during 1995. The audit covered a sample check of 26 procurement actions involving US$ 5.78 million (mostly relating to the year 1994), each involving $20,000 or more and hence requiring formal bidding processes as per financial rule 110.19. The main objectives of the audit were to assess the level of compliance with financial rules, regulations and existing procurement procedures and to determine whether the procurement was made in an economic and efficient manner.

2. On the whole, the extent of breaches of basic procurement control procedures noticed and other issues raised during the audit indicated the need to strengthen the planning, monitoring and control of the procurement process. The audit findings and recommendations were discussed with and reported to DDSMS. Management has taken or initiated the corrective actions recommended. The present report contains a summary of the major findings, recommendations and reactions thereto.

II. AUDIT FINDINGS AND RECOMMENDATIONS

A. Acceptance of facsimile bids compromising the confidentiality of the bidding process

1. Findings and recommendations

3. Financial rule 110.20 prescribes that all bids shall be publicly opened at the time and place specified in the invitation to bid and an immediate record made thereof. This implies that sealed bids should be obtained. However, in 13 out of 26 cases reviewed, the requirements of sealed bids and public opening of bids were either not communicated to the vendors or not complied with. As a result, there was frequent use of facsimile-transmitted bids. Although it may facilitate faster delivery of bids by vendors, the use of facsimile-transmitted bids could seriously compromise the confidentiality of the bidding process and encourage malpractice, if adequate precautions are not taken.

4. In order to prevent any possibility of a bid being disclosed prematurely, strict confidentiality of the bid should be maintained until opening. Article 28.5 (b) of the Model Law on Procurement of Goods and Construction referred to by the Contract and Procurement Service states that a tender may alternatively be supplied in any other form specified in the solicitation

document that provides a record of content of the tender and at least a similar degree of authenticity, security and confidentiality. A draft administrative instruction based on the Model Law was stated to be under preparation by the Office of Legal Affairs.

5. Although the audit team was informed that the Contract and Procurement Service had obtained a dedicated fax machine and a secure room in 1994 to ensure the confidentiality of fax bids, the staff member who handled the fax bids was not independent enough to assure the confidentiality. The audit team recommended that the practice of receiving facsimile bids for purchase involving $20,000 or more should be discontinued until the security and confidentiality of the bids could be fully assured.

2. Reactions

6. In response to the recommendation, the management stated that following on the draft audit report, action had already been taken to discontinue the use of facsimile to send and receive bid/proposal documents. It was further stated:

> "We will further review our procedures in this regard when the expected Office of Legal Affairs administrative instruction covering use of fax bids is issued; however, any reverting to use of fax bids will be strongly influenced by whether or not the staff situation will allow for 'independent' control of fax bids after receipt and before opening."

In this connection, acquisition of a fax machine that automatically seals the bids upon receipt could be considered.

B. Restrictive (non-generic) technical specifications inhibiting the competitive bidding process

1. Findings and recommendations

7. In accordance with the relevant Policies and Procedures Handbook, every effort should be made to draw up specifications that are generic or "neutral" since the requirements for competitive bidding obviously cannot be met if the specifications point towards one supplier.

8. The audit disclosed that in 46 per cent of the cases the technical specifications were either restrictive in nature or sole-source, and precluded or otherwise made extremely difficult a valid and practical competitive bidding process.

9. According to the Contracts and Procurement Service, it is not always possible for technical staff to deal in generic specifications because of host Governments' standardization, local maintenance facilities, experience and training of project staff favouring equipment of a certain manufacturer, known suitability of specific manufacturers products, and so on. However, the audit team pointed out that under the terms of financial rule 110.19 any

standardization of supplies and equipment has to be specifically approved on the advice of the Headquarters Committee on Contracts.

10. In one of the cases where the specifications used were restrictive in nature, the audit team found that besides the specifications being non-generic, which were described by unsuccessful vendors as restricted to the product of one source and of very old technology, there appeared to have been no objective technical evaluation of the bids and equal opportunity was not given to the lowest bidder to prove the reliability of the equipment with the user references given, while warranty was reduced to suit one bidder. Had this not been so, a saving of up to $36,500 could have been made in this case.

11. The audit team recommended:

(a) That it should be ensured by the Contracts and Procurement Service that the specifications drawn up by the technical advisers are generic in nature;

(b) That there should be independent scrutiny of the technical recommendations of the technical advisers and any pre-qualification exercise prior to the acceptance and award of contracts/purchase orders, which should provide equal opportunity to all the prospective suppliers;

(c) That any complaints by the bidders about the specifications should be examined by the Contracts and Procurement Service objectively and that should a non-lowest bid be proposed to be accepted as the "lowest acceptable bid", convincing reasons, taking account of such complaints, should be recorded and brought to the specific notice of the Headquarters Committee on Contracts;

(d) That any standardization of supplies and equipment, including vehicles, should be specifically approved on the advice of the Committee on Contracts, pursuant to financial rule 110.19.

2. Reactions

12. Agreeing with the recommendations, the management reported:

"To the maximum extent of staff resources available, Contracts and Procurement Service will work closely with Department of Development Support and Management Services technical officers in future to ensure the provision of generic specifications whenever possible, including critical review of those specifications. Scrutiny of technical recommendations made by Department for Development Support and Management Services substantive staff in regard to bids will be strengthened and every effort will be made to ensure equal opportunity be given to all prospective suppliers. In cases where the Headquarters Committee on Contracts becomes involved, full disclosure of the record of the bid exercise will be brought to the Committee's attention to assist in their deliberations. Contracts and Procurement Service will take steps to meet the requirement that the Committee

approve standardized purchases on the basis of United Nations financial rule 110.19."

C. Need to attain equitable geographical distribution in the procurement of equipment and supplies

1. Findings and recommendations

13. Pursuant to the terms of General Assembly resolution 2688 (XXV) of 11 December 1970, the principle of equitable geographical distribution, consistent with maximum effectiveness, should be observed in the procurement of equipment and supplies for the implementation of development programme assistance.

14. The audit team noted that in 12 out of 26 cases reviewed, requests or invitations to bid were not issued to vendors from developing countries. As vehicles and some of the equipment and supplies purchased from the developed countries are also available for purchase from developing countries in the regions concerned or outside, the audit team was unable to see any reason for the Contracts and Procurement Service not seeking out bids from vendors of developing countries. With the exception of the local country portion of implementation contracts, the audit team found no significant effort to attain geographical distribution in the procurement of equipment and supplies.

15. In a few cases, international vendors from developed countries who had established offices in project sites were considered by the Contracts and Procurement Service and the substantive officers of DDSMS in New York and the field as "local country companies" in their shortlists of potential vendors.

16. That position should be viewed in the context of what is stated in the relevant Policies and Procedures Handbook, which is as follows:

> "In keeping with the theme of 'New Dimensions' in technical cooperation and as a means of promoting technical cooperation among developing countries, efforts are made to increase the representation of firms from developing countries on the roster and in bidding with a view to promoting self-reliance of developing countries."

17. The Contracts and Procurement Service pointed out that during the period from 1992 to 1994, procurement from developing countries had averaged approximately 40 per cent of total purchases, including field and local purchases. However, the audit observations were limited to international procurement only. For instance, as mentioned in paragraph 21, the purchase of a certain compressor could have been made from a developing country at lesser cost. There is a need to demonstrate that the Contracts and Procurement Service is attempting to meet the requirements set for procurement in developing countries in its international procurement.

18. The audit team therefore recommended:

(a) That, with regard to international procurement, concerted efforts be made to identify potential vendors in the developing countries and to increase the representation of vendors from those countries in bidding and award of contracts in order to attain equitable geographical distribution in procurement of equipment and supplies, with a view to promoting self-reliance of the developing countries;

(b) That progress should be monitored separately and reviewed to take such corrective measures as may be necessary from time to time in order to reach the objective already set.

2. Reactions

19. In responding to the recommendations, management assured that they would establish and monitor a system to include firms from developing countries in their international procurement cases wherever possible and that they would enlist the help of the Inter-agency Procurement Services Office and the Office of Project Services in identifying likely firms.

D. Purchases through certain agencies involving serious risks, apparently at higher costs

1. Findings and recommendations

20. The audit team noted that the Contracts and Procurement Service had been inviting bids and making purchases from certain agencies that were apparently procurement brokers disguised as vendors. There were four such agencies. A review of the position of those agencies on the basis of Dun and Bradstreet reports provided by the Purchase and Transportation Service of the Office of Conference and Support Services revealed that they were mostly small with a poor or no credit appraisal rating and hence risky to do business with. Yet those agencies received a number of purchase orders involving large amounts. The total purchases made from 1988 to 1995 by United Nations Headquarters and not confined to those of the Contracts and Procurement Service amounted to $10.1 million.

21. These agencies would obviously not sell others' products without a commission. Therefore, the United Nations cannot be obtaining goods or services at competitive prices from them. For instance, the audit team noted that against a requisition for a project in a country in Asia, the purchase of a certain compressor manufactured in a neighbouring country was done through a procurement agency (in Europe). The audit team believed that this could have been done at a lesser cost, if only quotations had been directly requested from the manufacturers or dealers of the product. In the assessment of the audit team, based on review of a few cases, equipment and parts could have been obtained from manufacturers at a price that would be at least 20 per cent lower

than that of other sources. Even assuming a commission of 10 per cent, the United Nations may have paid an additional $1 million on the purchases mentioned in paragraph 20.

22. Some of the purchases through these agencies under unusual circumstances are dealt with in section E of the present report.

23. The audit team was informed by the Contracts and Procurement Service that:

> "Our basic policy for use of such sources, which we consider as non-exclusive wholesale vendors, is that they should be mainly used for equipment packages which are not available from any single supplier. The alternative would be to place the different orders on different suppliers, which would increase shipping cost, involve unacceptable time delays, etc., and would not necessarily lead to lower overall cost."

However, the audit team felt that, with improved planning of procurement, it should be possible to have consolidated procurement related to appropriate sources at lesser cost, rather than frequently using these "non-exclusive" vendors.

24. According to the Contracts and Procurement Service, at least three of the vendors are included in the Inter-agency Procurement Services Office's master database of preferred vendors and are being used extensively by various procurement agencies. However, in the assessment of the audit team based on this audit and a preliminary review in one of the peace-keeping missions, there are risks involved. It is necessary formally to consider the financial viability and standing of all suppliers and contractors on the roster and to update such appraisals regularly.

25. The Contracts and Procurement Service indicated that:

> "Introduction of the new computerized database of vendors which we are currently working on with the Purchase and Transportation Service will provide relevant information on the financial status of the companies with which we do business."

26. The audit team recommended

(a) That the Contracts and Procurement Service, in concert with the Purchase and Transportation Service of the Office of Conference and Support Services, reassess the credentials of these agencies and the risks involved in continued dealings with them, in the light of the audit findings, and take suitable action;

(b) That, bearing in mind the specific instance mentioned in paragraph 21, the manufacturers and authorized dealers of the products so far procured through these agencies should be identified in order to invite quotations/bids from them directly in the future.

2. Reactions

27. Indicating that the Contracts and Procurement Service had taken the necessary action, internally, to minimize (and even discontinue) dealings with the procurement agencies in question, the management stated:

> "We will be working with the Department for Development Support and Management Services requisitioners to eliminate 'mixed' procurement requests in future, and thereby we can focus more easily on manufacturers and authorized dealer sources."

Similar action will have to be taken by the Purchase and Transportation Service of the Office of Conference and Support Services.

E. Irregular acceptance of belated bids jeopardizing the credibility of the procurement process

1. Findings and recommendations

28. As mentioned earlier, financial rule 110.20 requires that all bids shall be publicly opened at the time and place specified in the invitation to bid and an immediate record made thereof. This clearly implies that late bids are to be rejected. However, the audit team noted, in its sample check, four instances where belated bids were not rejected, but given full consideration. In three of these cases, belated fax bids of three of the procurement agencies mentioned in section D above were accepted.

29. The following were noticed in the procurement of mining and other equipment through a purchase order for $99,800 placed with a purchasing agency after acceptance of its belated offer:

(a) The requisitioning document issued by the substantive unit had already recommended the particular purchasing agency. The Procurement Officer concerned had shown undue familiarity in that a personal greeting of "Happy Holidays to all" was added by him in the request for quotation addressed to the vendor. In this connection, there would appear to be a need to clarify the boundaries between acceptable and unacceptable behaviour of procurement staff;

(b) Specifications were vague, generally lacking even the basic details needed to request vendors to provide quotations. It appeared that the requisition was based on a catalogue or other product or price list available from the purchasing agency;

(c) Quotations were requested from only three procurement agencies; two responded and one quotation was considered incomplete. It was not clear why quotations were not invited from any manufacturer or authorized dealer. According to the Contracts and Procurement Service, the detail of specifications put forward by project field staff plus the "mixed" nature of the items to be purchased was the reason.

30. The audit team recommended

(a) That, as required under financial rule 110.20, all bids should be publicly opened at the time and place specified in the invitation to bid and an immediate record made thereof, whether bidders' representatives are present or not;

(b) That the practice of accepting late bids be stopped immediately;

(c) That, in order to project a proper image of the procurement staff, undue familiarity with any prospective vendor should be discouraged.

2. Reactions

31. The management reported that the recommended actions vis-à-vis bid openings, late bids and salutations had already been taken. The audit team noted that on the basis of the draft audit report and the discussions held the Contracts and Procurement Service had put in place measures to strengthen the procedures and instructed all the procurement and contracts officials, among other things, (a) to eliminate entirely the acceptance of late quotations/ bids/proposals (received after set date) regardless of circumstances and properly to secure all bids/proposals until the prescribed opening date; (b) to ensure that the opening was witnessed by at least one other staff member and possibly a technical officer, both of whom were to sign the abstract of bids; and (c) to avoid the appearance of overfamiliarity with vendors.

F. Non-maintenance of vendor files, thereby frustrating audit and management reviews

1. Findings and recommendations

32. For the registration of potential vendors, an application should be submitted on the vendor registration form, containing relevant data for review. Additional documentary evidence, such as financial statements, references, and so on should be attached to the registration form. The vendor files should contain these and all vendor evaluations, complaints and other information.

33. The vendor files are important for any future review of vendors that may be warranted. They are also an important audit trail. These files are part of what is generally called the "permanent files" of any procurement office. The audit team was informed that none of these files were kept by the Contracts and Procurement Service. Computer printouts on vendors available on request were found to provide some information that was also available in the vendor roster. Shortage of space was mentioned as one of the reasons for disposing of vendor files. Further, it was indicated that it was a fire warden's decision to dispose of files.

34. In the absence of vendor files with comprehensive documentation, there is no audit trail for review and evaluation with regard to how vendors were registered, what their qualifications and financial status were at the time of

registration and what deficiencies have been reported subsequently. At the same time, management lacks information for review of vendors' performance.

35. The audit team recommended that arrangements be made to reconstruct the vendor files to the extent possible and from now on to maintain the files properly and in a comprehensive manner, including vendor evaluations, complaints and so on.

2. Reactions

36. The management reported:

> "We will be studying the best method to re-establish our vendor files, after discussing the matter with Purchase and Transportation Service. This is an opportune time to start this exercise since the Purchase and Transportation Service and the Contracts and Procurement Service are involved in a joint re-registration of vendors and contractors."

This has to be expedited.

G. Doubtful propriety of assistance involving additional project expense in ensuring a vendor's compliance with the terms for award of contract

1. Findings and recommendations

37. A contract for the purchase of solar modules for a project in a country in Africa was awarded to a non-lowest bidder. Earlier, in the presentation of the case to the Headquarters Committee on Contracts in August 1994, the Contracts and Procurement Service had among other things stated that only that bidder offered to provide the necessary training in the installation, operation and maintenance of solar equipment in the project area.

38. The invitation to bid in this case required:

> "The international suppliers should either have technically qualified enterprises or have the capability and experience to deal with local enterprises and provide them with the necessary training and support. The national suppliers should have the technical capabilities and experience in the area of solar installations and services and a support link with an international manufacturer."

Further, it was required that, in order to ensure the availability and provision of warranty services by the suppliers in the host country, some sort of contractual agreement between the international suppliers and the local enterprises should be part of the supply contract.

39. A review of the procurement file disclosed that at the time of closing of bids on 1 March 1994, the local representatives of the non-lowest bidder had no offices in the project area. However, there was evidence of a strong attempt to

facilitate the otherwise missing presence of that vendor in the project area by helping to negotiate and secure, and even draft an agency agreement between the vendor company and its agents in the project area, during a study tour of the National Project Director. The tour was undertaken "to discuss and formulate the terms and conditions of a contractual agreement between the international supplier of equipment and their local partner enterprises ... which is important to be included in the forthcoming supply contract with the supplier". This was a vendor responsibility. A contract between the vendor and their subcontractors was not to be negotiated, incurring costs.

40. It was clarified by the Contracts and Procurement Service that the Project Director's

> "... travels and assistance given to the vendor was designed to do what was considered by the [host country] Government to be in the best interest of the project. His travel was paid from project funds under study tour arrangements, but since this project is government-executed, this is standard procedure in that the Government dictates the use of its own funds; and it should be noted that this was done without any consultation with the Contracts and Procurement Service whatsoever."

However, the audit team was doubtful of the propriety of undertaking a "study tour" for the purpose stated and of meeting the cost from project funds. Since procurement is the responsibility of the Contracts and Procurement Service, irrespective of the source of funding, observance of certain norms will have to be ensured.

41. The audit team therefore recommended that the propriety of the assistance involving additional expense to the project in ensuring a vendor's compliance with the terms of the invitation to bid for award of contract may be examined with a view to issuing policy instructions clarifying the position for all concerned.

2. Reactions

42. In response to the recommendation, the management indicated that they would appraise the various substantive divisions within DDSMS of the concerns regarding funding of project study tours and so on, which may have a direct impact on vendor compliance with the terms of the invitation to bid and the subsequent award of a contract. The precise action taken by DDSMS in this regard is awaited.

H. Possible conflict of interest in the engagement of a consultant to assist in the preparation of specifications and the technical evaluation of bids

1. Findings and recommendations

43. A requisition was raised in April 1994 for the purchase of three underground longhole drilling systems for a certain project. A corporate entity was contracted to design the underground drilling system, prepare specifications and assist in evaluating the bids received.

44. The consultant company was required to be independent in order to prepare generic specifications and assist in technical evaluation of bids to allow for an objective procurement process. However, it also suggested four vendors. One of the vendors suggested was a corporation that had business dealings with the consultant company. The latter had supported the corporation in a purchase around the time that the corporation was awarded the contract. There was a possible conflict of interest, although in this case the corporation's bid was not accepted. It was not clear whether the consultant company had any business dealings with the other vendors recommended by it.

45. A list of eight potential bidders was made (four were added to those recommended by the consultant). A call for bids was issued and three bids (only of those vendors who were recommended by the consultant, including the corporation's bid) were received. The non-submission of a bid by any of the four vendors who were not recommended by the consultant raises doubts about the nature of the specifications. After changing technical specifications, a re-bid exercise was made with the vendors who had submitted bids earlier. Out of the three bidders, only two resubmitted bids. Ultimately, the contract was awarded at a price of $2.4 million.

46. As regards the propriety of the consultant recommending vendors, the Contracts and Procurement Service stated that while the consultant company went beyond the letter of its terms of reference in recommending sources, this was acceptable and necessary in this case. It is the considered view of the Office of Internal Oversight Services, however, that the services provided by a consultant engaged to assist in the preparation of specifications and the evaluation of bids should not extend to suggesting vendors for inviting bids.

47. In view of the fact that the consultant company went out of the way to recommend vendors and that the specifications prepared by it did not elicit any bid from any vendor not recommended by it and of the apparent conflict of interest in this case, the audit team recommended

(a) That in the future, whenever it is necessary to engage a consultant, corporate or individual, the credentials of the proposed consultant should be properly verified to ensure that there is no conflict of interest;

(b) That in no case should a consultant engaged to prepare specifications and assist in technical evaluation be allowed to recommend vendors for invitation to bid.

2. Reactions

48. Accepting the recommendations, the management indicated that they would revise their contracting procedures regarding consultants and would properly address the concerns as regards potential conflict of interest in relation to the initial hiring of consultants and their participation in the shortlisting of vendors.

III. CONCLUSION

49. It is expected that, as a result of this audit and follow-up, DDSMS will strengthen the planning, monitoring and control of the procurement process and thereby enhance the integrity of the process, diversify better the sources of procurement and improve cost-effectiveness. There is, however, a need for reorganization of the Contracts and Procurement Service in view of the continued decline in its workload.